

# Report of the auditor-general to the Free State Legislature and the council on the Metsimaholo Local Municipality

## Report on the audit of the financial statements

### Qualified opinion

1. I have audited the financial statements of the Metsimaholo Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2019, the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion section of this auditor's report, the financial statements present fairly, in all material respects, the financial position of the Metsimaholo Local Municipality as at 30 June 2019, and its financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2018 (Act No. 1 of 2018) (Dora).

### Basis for qualified opinion

#### Property, plant and equipment

3. I was unable to obtain sufficient appropriate audit evidence for property, plant and equipment as the municipality did not maintain an adequate asset register and could not provide me with supporting records for disposals. I was unable to confirm property, plant and equipment by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to property, plant and equipment stated at R1 390 096 253 (2018: R1 359 565 341) in note 11 to the financial statements. In addition, the municipality did not correctly classify various items of property, plant and equipment between the classes of assets as reflected in note 11, in accordance with GRAP 17, *Property, plant and equipment*. I was unable to determine the full extent of the misclassifications as it was impracticable to do so.
4. The municipality also did not disclose property, plant and equipment in accordance with GRAP 17, *Property, plant and equipment*. Infrastructure projects which have been finalised as at 30 June 2019 were incorrectly included in the closing balance of work-in-progress as reflected in the reconciliation of work-in-progress in note 11 to the financial statements. Consequently, work-in-progress was overstated by R123 353 761.

#### Investment property

5. I was unable to obtain sufficient appropriate audit evidence for investment property as the municipality did not maintain an adequate asset register and could not provide lease agreements. I was unable to confirm investment property by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to investment property

stated at R295 200 836 (2018: R295 221 476) in note 10 to the financial statements. In addition, the municipality incorrectly classified properties that do not meet the definition of investment properties as outlined in GRAP 16, *Investment property*. Consequently, investment property is overstated by R58 004 887. There was also a resultant impact on the surplus for the period and on the accumulated surplus.

### **Irregular expenditure**

6. The municipality did not disclose all instances of irregular expenditure incurred in the notes to the financial statements, as required by section 125(2)(d) of the MFMA. The municipality made payments in contravention of the supply chain management (SCM) requirements and made overtime payments not in line with the municipality's overtime policy, which were not disclosed. I was unable to determine the full extent of the understatement of irregular expenditure stated at R58 040 885 in note 51 to the financial statements as it was impracticable to do so.

### **Service charges**

7. I was unable to obtain sufficient appropriate audit evidence that all service charges had been properly accounted for, due to the status of the accounting records. I could not confirm that consumer debtors registered as indigent, did qualify for indigent status in terms of the municipality's indigent policy. I was unable to confirm the service charges by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to service charges stated at R698 481 721 in note 22 to the financial statements.

### **Property rates**

8. I was unable to obtain sufficient appropriate audit evidence that all property rates had been properly accounted for, due to the status of the accounting records. I could not confirm that consumer debtors registered as indigent, did qualify for indigent status in terms of the municipality's indigent policy. I was unable to confirm the service charges by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to property rates stated at R143 648 432 in note 26 to the financial statements.

### **Depreciation and amortisation**

9. The municipality did not correctly provide for depreciation on items of property, plant and equipment in accordance with GRAP 17, *Property, plant and equipment*. The depreciation was calculated using the incorrect useful lives. Consequently, depreciation and amortisation included in note 32 to the financial statements is understated by R13 727 130 and property, plant and equipment included in note 11 to the financial statements is overstated by R13 727 130.

### **Public contributions and donations**

10. I was unable to obtain sufficient appropriate audit evidence that all public contributions and donations received have been accounted for in accordance with GRAP 23, *Revenue from non-exchange transactions*. Donations reflected on third party confirmations could not be traced to the accounting records of the municipality and I could not confirm if the municipality actually received the donated assets or services. I was unable to confirm public contributions and donations by alternative means. Consequently, I was unable to determine whether any

adjustments were necessary to public contributions and donations stated at R25 690 347 in note 28 to the financial statements.

### **Context for the opinion**

11. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of this auditor's report.
12. I am independent of the municipality in accordance with sections 290 and 291 of the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* and, parts 1 and 3 of the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA codes), as well as the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA codes.
13. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

### **Emphasis of matters**

14. I draw attention to the matters below. My opinion is not modified in respect of these matters.

#### **Unauthorised expenditure**

15. As disclosed in note 49 to the financial statements, unauthorised expenditure of R77 564 428 was incurred, due to overspending of a vote in the approved budget.

#### **Fruitless and wasteful expenditure**

16. As disclosed in note 50 to the financial statements, fruitless and wasteful expenditure of R22 372 735 (2018: R2 255 167) was incurred, mainly due to interest on arrear payments to creditors and the payment for work not performed.

#### **Restatement of corresponding figures**

17. As disclosed in note 46 to the financial statements, the corresponding figures for 30 June 2018 were restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2019.

#### **Material uncertainty relating to claims against the municipality**

18. With reference to note 43 to the financial statements, the municipality is the defendant in various claims against the municipality. The municipality is opposing these claims. The ultimate outcome of these matters could not be determined and no provision for any liabilities that may result were made in the financial statements.

### **Material losses**

19. As disclosed in note 36 to the financial statements, material water losses of R30 300 137 (2018: R16 307 842) and electricity losses of R10 352 646 (2018: R15 686 341) were incurred by the municipality mainly due to internal use, illegal connections and supply to informal areas.

### **Material impairment**

20. As disclosed in note 7 to the financial statements, consumers and other receivables were impaired by R1 290 138 259 (2018: R1 091 545 789).

### **Other matter**

21. I draw attention to the matters below. My opinion is not modified in respect of these matters.

### **Unaudited disclosure notes**

22. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

### **Unaudited supplementary schedules**

23. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion on thereon.

### **Responsibilities of the accounting officer for the financial statements**

24. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and Dora, and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
25. In preparing the financial statements, the accounting officer is responsible for assessing the Metsimaholo Local Municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

### **Auditor-general's responsibilities for the audit of the financial statements**

26. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.



27. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

## Report on the audit of the annual performance report

### Introduction and scope

28. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected key performance areas (KPAs) presented in the annual performance report. I was engaged to perform procedures to raise findings but not to gather evidence to express assurance.
29. I was engaged to evaluate the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected key performance area presented in the annual performance report of the municipality for the year ended 30 June 2019:

KPA	Pages in the annual performance report
KPA 1 – service delivery and infrastructure development	x – x

30. The material findings in respect of the usefulness and reliability of the selected KPAs are as follows:

### KPA 1 – Service delivery and infrastructure development

#### Various indicators

31. I was unable to obtain sufficient appropriate audit evidence for the reported achievements of the indicators listed below. This was due to limitations placed on the scope of my work. I was unable to confirm the reported achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements in the annual performance report of the indicators listed below:

Indicator description	Reported achievement
Number of kms of internal roads repaired and maintained	Target not achieved - only pothole patching done – 2 236 m2
Number of km of roads identified for paving and storm water construction	Target achieved - construction has been completed
Number of kms of roads graded	Target achieved - 26.8 km of road graded

Indicator description	Reported achievement
% compliance with the blue drop water quality accreditation system	Target not achieved
% compliance with the green drop quality accreditation system	Target not achieved
Refuse removal service extended to all new formal settlements as per township register within Metsimaholo LM.	Target achieved - 100% refuse is collected on all formal and informal household, businesses and industries on a 5 and 6 days basis.
Illegal dumping sites removed	Target achieved - 12 illegal dumping sites were removed
% of fire and disaster incidents within the municipality attended	Target achieved

#### Upgrade the Waste Water Treatment Works (WWTW)

32. The achievement for the target to upgrade the WWTW reported in the annual performance report was 40%. However, the supporting evidence provided did not agree to the reported achievement and indicated an achievement of 54%.

#### Various objectives

33. The following strategic objectives approved in the service delivery and budget implementation plan (SDBIP) were not consistent with the strategic objective reported in the annual performance report.

Strategic objective (SDBIP)	Strategic objective per annual performance report
Ensure the development and annual review of the municipality's comprehensive infrastructure plan (CIP)	To ensure that the municipality broadly delivers service according to the strategic orientation based on key sector plans.
To ensure development of legally compliant and credible IDP (included under KPA 1)	To ensure development of legally compliant and credible IDP (included under KPA 4)

#### Percentage compliance with the green drop water quality accreditation system

34. The target approved in the SDBIP was >99%. However, the target reported in the annual performance report was target not achieved.

## **Other matter**

35. I draw attention to the matter below.

### **Achievement of planned targets**

36. Refer to the annual performance report on pages xx to xx for information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 31 to 34 of this report.

## **Report on the audit of compliance with legislation**

### **Introduction and scope**

37. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

38. The material findings on compliance with specific matters in key legislations are as follows:

### **Annual financial statements**

39. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of current assets, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.
40. The 2017-18 annual report was not tabled in the municipal council after the end of the financial year, as required by section 127(2) of the MFMA.

### **Expenditure management**

41. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The expenditure disclosed does not reflect the full extent of the irregular expenditure incurred as indicated in the basis for qualification paragraph.
42. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R22 372 735, as disclosed in note 50 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. Fruitless and wasteful expenditure amounting to R21 647 454 was incurred on the Oranjeville sports complex.
43. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R77 564 428, as disclosed in note 49 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by overspending of votes in the approved budget.

44. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.

#### **Revenue management**

45. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.

#### **Asset management**

46. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA.
47. All investments were not made in accordance with the requirements of the investment policy as cash flow projections and regular credit checks were not performed, as required by municipal investment regulation 3(3).

#### **Strategic planning and performance management**

48. The performance management system and related controls were inadequate as it did not describe how the performance planning, monitoring, measurement, review and reporting processes should be conducted and managed, as required by municipal planning and performance management regulation 7(1).

#### **Procurement and contract management**

49. Some of the goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, in contravention of by SCM regulation 17(a) and (c). Similar non-compliance was also reported in the prior year.
50. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1). Similar non-compliance was also reported in the prior year.
51. Sufficient appropriate audit evidence could not be obtained that a construction contract was awarded to contractors that was registered with the Construction Industry Development Board (CIDB) in accordance with section 18(1) of the CIDB Act, 2000 (Act No. 38 of 2000).
52. Some of the quotations were accepted from bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
53. Some of the quotations were accepted from bidders whose tax matters had not been declared by the South African Revenue Service to be in order, in contravention of SCM regulation 43.
54. Sufficient appropriate audit evidence could not be obtained that the performance of contractors or providers was monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.



- 55. The preference point system was not applied on some of the procurement of goods and services above R30 000 as required by section 2(a) of the Preferential Procurement Policy Framework Act, 2000 (Act No. 5 of 2000).
- 56. Some of the invitations for competitive bidding were not advertised for a required minimum period of days, in contravention of SCM regulation 22(1) and 22(2).
- 57. Contracts were awarded to bidders based on points given for criteria that differed from those stipulated in the original invitation for bidding, in contravention of SCM regulations 21(b) and 28(1)(a) and the Preferential Procurement Regulations.
- 58. Bid specifications for some of the tenders were drafted in a biased manner and did not allow all potential suppliers to offer their goods or services, in contravention of SCM regulation 27(2)(a).

#### **Human resource management**

- 59. Appropriate systems and procedures to monitor, measure and evaluate performance of staff were not developed and adopted, as required by section 67(1)(d) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).
- 60. An approved staff establishment was not in place, as required by section 66(1)(a) of the MSA.

#### **Consequence management**

- 61. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) of the MFMA.
- 62. Irregular expenditure incurred by the municipality were not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.
- 63. Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.

#### **Conditional grants**

- 64. Performance in respect of programmes funded by the regional bulk infrastructure grant was not evaluated within two months after the end of the financial year, as required by section 12(5) of the Dora.

<b>Other information</b>
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- 65. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report and the selected KPA presented in the annual performance report that have been specifically reported in this auditor's report.
- 66. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.

67. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected KPA presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
68. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate. However, if it is corrected this will not be necessary.

### **Internal control deficiencies**

69. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion, findings on the annual performance report and the findings on compliance with legislation included in this report.
70. Inadequate governance by the council to address and conclude on the suspension of the municipal manager, which was suspended for the entire financial year under review as well as during the current audit. All the positions of the managers reporting directly to the municipal manager were also vacant for the mentioned periods. This resulted in various officials acting in these vacant positions, contributing to the instability in the leadership of the municipality. At the time of finalising this report, none of these vacancies was filled and the municipal manager was still on suspension.
71. Leadership did not monitor and enforce the implementation of the corrective measures included in the audit action plan to address the weaknesses relating to the finance and SCM directorates with regard to asset management, procurement and contract management, as well as the prevention of irregular, fruitless and wasteful expenditure.
72. A lack of commitment of key officials and staff supporting them regarding the implementation and monitoring of internal controls over daily and monthly processing of transactions resulted in material audit findings included in this report.
73. Inadequate oversight and accountability resulted in officials not being held accountable for transgressions with laws and regulations and an increase in the number of non-compliance findings raised during the year under review.
74. Ineffective monitoring and supervision over financial and performance reporting resulted in internal control deficiencies that were not identified, communicated and corrected in a timely manner.

75. There was a lack of commitment to prioritise and implement standard operating procedures to manage processes for performance reporting, including the safeguarding of information and effective monitoring and evaluation of reported performance information.

*Auditor-General*  
Bloemfontein

29 November 2019



AUDITOR-GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*

## **Annexure – Auditor-general's responsibility for the audit**

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for the selected KPA and on the municipality's compliance with respect to the selected subject matters.

### **Financial statements**

2. In addition to my responsibility for the audit of the financial statements as described in this auditor's report, I also:
  - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control
  - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control
  - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer
  - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Metsimaholo Local Municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor's report. However, future events or conditions may cause a municipality to cease continuing as a going concern
  - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation

### **Communication with those charged with governance**

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.